

Answers to Post-Presentation Questions for Steve Shaw

How often do these discounts occur?

On slides 35 and 36, I showed a distribution of bond prices that illustrated the percentage of investment grade corporate bonds trading at a premium and discount to par value. Bond prices have rallied since the March 19, 2020 chart, so, today, there are far fewer bonds trading at discounts to par value.

Do corporate bonds pay regular dividends?

live answered

Are you teaching us how to do this on our own, or do we need to subscribe to your service?

live answered

When you buy a bond, do you look for YTM at first and hope for cap gains or do you actually assume cap gains based on interest rate outlook or prospects of company (i.e., you think bond is underpriced)?

We are focused on total return, so we identify bonds that offer a compelling YTM plus opportunities for capital appreciation. Since we continually update our recommendations based on company performance and the pricing of the bonds relative to others, we are able to evaluate the likelihood of further capital appreciation and update our buy/sell/hold recommendations accordingly.

Can you buy bonds on margin i.e. can you buy \$20K of bonds with \$10K in savings?

live answered

With rates so low now, how reasonable is it to assume cap gains going fwd - seems like risk is for cap loss in long bonds (except for the lowest grade bonds).

live answered

How liquid are the bonds of major companies?

Discussed on slide 20 of the presentation.

Also, can you speak to wide bond price spreads, especially on lower quality stuff during downturn - hard to trade when you're on wrong side of spread.

We discussed typical bid-ask spreads on slide 20 of the presentation. There were wide bid-ask spread in both high- and low-credit-quality bonds during the COVID-19 crisis. We did not sell one bond when markets were falling in March. Instead we held our positions and, in certain cases, recommended purchasing additional bonds that had fallen in price.

Is it rare to buy a bond at premium? When should you buy a bond at premium?

Sometimes we do buy bonds at premium to their par value. We do this in cases where we believe such bonds are still a compelling relative value to other corporate bonds available in the marketplace.

Can you place limit orders to buy bonds (not at Vanguard, unfortunately). If you don't like spread or price, you have to constantly check vs bidding "your price" online and hoping it gets hit.

Yes, for certain platforms such as Fidelity, all orders are entered as limit orders. If you enter your limit order at the quoted price, the trade will be filled ~98% of the time. If you enter a limit order between the bid-offer spread, the likelihood of trade execution is much lower and depends on the size and price of the limit order and the trading activity of the particular bond.

Do bullet shares have any advantages?

Our focus is individual corporate bonds, so I can't speak to the advantages of different bond funds. All bond funds, regardless of flavor, face the same disadvantages I discussed in slides 9-13.

Why the comparison to VBTLX instead of the Total corp bond VTC?

On slide 11, we showed the largest bond funds in the world, as funds like these are where most investors are putting their fixed income investments. Vanguard's VTC ETF only held \$500 million as of June 30, 2020 compared to over \$200 billion for the Vanguard Total Bond Market Funds.

Is there more risk on 144a bonds relative to the same bond that's not 144a?

It wouldn't be 'the same bond' since the 144a issuance is a different bond than those issued by the same company that are not 144a issuances. It all depends on the provisions of the specific bonds.

How does bond liquidity compare to preferred shares?

We discussed corporate bond liquidity on slide 20. We are not aware of the quality of liquidity available in preferred stocks.

If you hold the individual bonds over a longer duration will it even out the risk to principal?

That's too general of a statement. The risk of permanent capital loss is driven by the potential of a default and not how long a bond is held.

What do you think of bonds with complex provisions eg. callable bonds, convertible bonds?

We don't invest in convertible bonds, and they represent a very small portion of the fixed income market. Many high-yield corporate bonds are callable at a premium prior to maturity. If buying bonds at a discount, this can work in the investor's favor. Investors must be careful when buying bonds at a premium and when the bond is callable prior to maturity at a materially lower price than that at which the investor is buying the bond.

What is the barrier to entry for some Vanguard like company to make a Science and tech bond fund etc?

Bond fund construction is not my area of expertise. It's hard to speculate on whether there would be a large appetite for such funds given the popularity of 'total market' bond funds

As a newbie to corp bonds, what's the take-home message with Bill Gross?

I'm not aware of Bill Gross recently speaking about individual corporate bonds.

How are bond interest payments taxed, comparing to favored tax treatment of stock dividends?

If held in a taxable investment account, corporate bond interest is taxed as ordinary income.

I guess he'll talk later about bond trading platforms?

*We recommend using either Fidelity or E*TRADE to invest in individual corporate bonds.*

Is the speaker going to give some corporate bond recommendations, given the current market volatility?

Our corporate bond recommendations are exclusive to BondSavvy subscribers:

<https://www.bondsavvy.com/investing-in-corporate-bonds>

Charts? *You can find charts of historical bond prices on Fidelity.com (if you are a Fidelity customer). You can also find historical bond prices by clicking this link:*

<http://finra-markets.morningstar.com/MarketData/Default.jsp?sdkVersion=2.55.0>

Would like to hear Steve's opinion on Closed End Corporate bond funds, eg PIMCO CEFs. Or Corp Bond CEFs in general. Thanks!

My focus is individual corporate bonds.

As an individual investor, I've found it difficult to buy the initial offerings. Should I not even try and just go to the secondary market?

Our focus is on secondary market corporate bonds.

Do you see any value in perpetual bonds, emerging market sovereign, corporate?

Our focus is individual corporate bonds issued by companies that file with the US Securities and Exchange Commission. It's where our expertise lies. There could be opportunities in other types of bonds, but those are not our areas of expertise.

What is the cost of buying and selling individual bonds? Seems like it is very opaque. Does it vary a lot between Schwab, Fidelity etc. Are there better sites as far as buying/selling cost is concerned?

*We discussed markups and markdowns corporate bond investors pay on slide 17. Schwab, Fidelity, and E*TRADE charge similar fees. Bond pricing for individual corporate bonds is transparent. Watch my 2018 presentation to the SEC here: <https://www.bondsavvy.com/fixed-income-investments-blog/corporate-bond-prices>*

What about actively managed bond ETFs with a reasonable expense ratio? For example, First Trust.

All bond funds owning hundreds of bonds face the same challenges I discussed with the larger bond funds on slides 9-13.

What recovery do you see in Hertz, is it better in general to take loss or wait?

We stayed away from the Hertz bonds due to the company's lack of EBITDA. We haven't done analysis on the potential recoveries for bondholders.

Are there opportunities in stable interest rate environment as well as rising interest rate environment? I know in falling interest rate environment, prices go up.

I discussed the drivers of corporate bond prices on slide 24. As discussed on slide 33, market interest rates generally do not impact high-yield corporate bonds. Given how low rates have fallen during 2020, finding 'bargains' in investment-grade-rated corporate bonds is difficult at this time.

is trend following applicable to bonds?

Understanding historical prices is part of our analysis, as we want to invest at compelling values. A number of factors determine when we recommend selling previously recommended bonds, and we discuss these in this blog post: <https://www.bondsavvy.com/fixed-income-investments-blog/when-to-sell-bonds>

Any tempting energy bonds that can survive LT low oil prices?

We did not make specific recommendations during this presentation. These are exclusive to BondSavvy subscribers.

Even if bond value goes down are you always guaranteed to receive back your principal no matter what?

You get repaid so long as the bond issuer does not default.

Alibaba trades as a safe dollar bond, is it true even considering country risk?

I haven't looked into the Alibaba bonds.

Do you have a subscription service which recommends bonds to buy and sell on a weekly or monthly basis?

What is the cost? Do you also manage bond portfolios?

<https://www.bondsavvy.com/investing-in-corporate-bonds>

Do you use credit sights or gimme credit services, are they expensive?

We do not use these other services.

Can you explain Coupons please?

We discussed coupons on slide 16 of the presentation.

Are there dedicated market makers on bonds?

Yes, there are over 100 corporate bond market makers that provide live bid/offer quotes to the various brokerages.

Do you ever speculate with bonds trading flat?

Typically not. We invest across the credit spectrum, but distressed debt investing is not our area of expertise.

What factors determine when a bond sells for more or less than its face value? The same factors that determine when a stock goes up or down or something else?

We discussed the key drivers of bond price movements on slide 24

So YTM is the right measure not the current yield, correct?

Investors need to consider both. One isn't more 'right' than the other, as they show the investor different things.

Please explain the concept of duration and its effect on value

Discussed on slide 32

Is there an easy way to calculate return when a bond is called?

live answered

Can one buy individual corporate bonds on Vanguard?

Yes

Any thoughts on Royal Caribbean bonds?

We have stayed away from these bonds for now.

Do you think the market reacts to ratings changes, or more often than not anticipates them and investors reprice bonds before ratings change? Also any comment on some wide split ratings? Moodys seems stricter these days?

live answered

Is your strategy consistent with practice of using bonds to diversify risk of equity portfolio? How many individual bonds must you hold to build a bond portfolio?

Not necessarily. We don't make individualized recommendations, so each subscriber will have a different equity / bonds / cash mix. We recommend building a bond portfolio over time rather than doing a 'big bang.' You can start investing in corporate bonds with one CUSIP and then add to this over time.

A few questions...

Is the worst case risk for bonds the risk of a company being unable to pay the bond off/bankruptcy?

As bonds approach maturity the price should converge to par value, right?

Would a screen for bonds be to look for bonds that are trading at a discount that are near dated in companies that have adequate financials/prospects to pay off or refinance the bond?

What would be an ideal maturity to trade? <1yr, <3yr, <5yr? A few questions...

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a) Yes

b) Yes, however, bond prices can continue to move based on the financials of the company, its ability to redeem the bond at maturity, and market conditions

c) Investors can have different strategies. We prefer owning bonds that don't all have similar maturity dates.

d) We identify bonds across the maturity spectrum that have the opportunity for capital appreciation. We don't recommend investing in bonds solely because they have a specific maturity date.

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How do you find the most reliable way to find out the corporate finances and what bonds they offer? Thank you!
You can find company financials on the investor relations sites of bond issuers. If you have a brokerage account, you can search for corporate bonds of a specific issuer to see which bonds they have previously issued and which bonds are available to be bought and sold.

Are your bond recommendations based purely on a company's fundamentals, or do you also weigh factors that measure market sentiment, macro, etc.?

We discussed our investment approach in slides 27-32 of the presentation.

What is your Opinion on the coziness of rating agencies and investment bankers?

We discussed our opinion on credit rating agencies on slides 21-23. We believe the biggest issue with credit rating agencies is the flawed methodologies employed to rate corporate bonds and that a bond rating does not speak to the relative value of a bond and whether a bond is a compelling investment.

Did S&P restore Treasuries to AAA? Did you agree with their downgrade to AA several years ago?

I believe S&P currently rates US Treasury bonds AA+. Given the country's debt levels and high deficit spending, I believe AA+ is a highly lofty rating for US Treasuries.

Most of my portfolio is tied up in Traditional and Roth IRAs. Can you buy these bonds with, say Traditional IRA money, without incurring tax consequences?

You can purchase individual corporate bonds in an IRA brokerage account. Your brokerage firm can help you roll the money into the IRA brokerage account.

Does interest coverage ratio consider corporate dividend payments?

We discussed interest coverage and its formula on slide 28 of the presentation. The denominator is interest expense on the company's debt. Stock dividend payments are not part of interest coverage.

Is tax treatment on capital gains same as stocks, any strategies on tax harvesting?

Capital gains treatment works similar for corporate bonds and stocks. Our goal is to maximize the pre-tax total return of each recommended corporate bond. This drives our analysis on when to sell a bond and not any tax-harvesting strategy.

Any alternatives to big rating agencies, credit sights?

BondSavvy is the best alternative in my opinion :)

Is there and Fund that uses your method?

We do not know.

What do base your decision on whether the bond has run far enough to sell?

Please read our blog post that discusses how we decide when to sell bonds: <https://www.bondsavvy.com/fixed->

income-investments-blog/when-to-sell-bonds

How do you decide when to bail and SELL a bond that has gone the wrong way (DOWN)?
live answered

This active bond investing method sounds easy, but how reliably can you produce significant gain in all the bond portfolio invested? Thank you!

Every bond will not produce 'significant gain,' but, thus far, we have shown how a select portfolio of individual corporate bonds can outperform the leading bond ETFs. Please see our investment returns here:
<https://www.bondsavvy.com/bond-investment-returns>

Please Comment on the accounting for taxes for accumulated interest and gains /losses!

If held in a taxable account, interest income is taxed as ordinary income. Capital gains are handled as they are for stocks and factor in short- and long-term capital gains.